



UK inflation is up again

UK inflation is up again, hitting 2.5% in the year to June, as the unlocking of the UK economy continues with prices rising faster than expected. The CPI measure of inflation rose from 2.1% in May and is above the Bank of England's 2% inflation target for a second consecutive month and is the highest rate for nearly 3 years. This latest rise will continue to fuel the debate about whether the Bank of England need to consider increasing interest rates in order to cool the economy.

A lot of this lies with comparisons with prices that were falling a year ago at the height of the lockdown. Bottlenecks in supply are also driving prices up. For instance, car manufacturers cannot find microchips, so cannot build enough new cars, so used car prices went up 4.4% in a month. During the pandemic, the microchip market switched its supply to electronics amid a slump in car sales. Some of the increase is from temporary effects, such as rising fuel prices which continue to increase inflation, while food from shops, eating and drinking out and clothing and footwear, usually cheaper at this time of year, went up in price instead as prices are recovering from the lows earlier in the pandemic.

There are plenty of examples like this, and the net result is that inflation is likely to be heading above 3% in the coming months. This is suitably above target to prompt a letter of explanation from the governor of the Bank of England to the chancellor, but we don't expect to see an immediate rise in interest rates from this.

Inflation should reach the peak at this level prior to falling back to normal, as the economy further reopens. It is, right now, high and climbing, but not out of control. And the reasons for this global rise are clear: demand is rebounding quickly after the pandemic, while supply is taking a little longer to ramp back up.

The MPC majority view is that the current inflation surge is transitory and is likely to reach a peak of 3%, but not much higher. Interest rates would therefore remain at the current record low of 0.1% throughout next year as inflation would then be expected to ease quickly in 2022, returning to the Bank's 2% target in the second half of next year.

Market Snapshot (09.07.21 – 16.07.21)

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FTSE 100	7008.09	↓1.60%	UK	0.60	↓6.25%	£/\$	1.3770	↓0.94%	Brent Crude	\$73.30	↓3.02%
S&P 500	4327.16	↓0.97%	US	1.25	↓6.02%	£/€	1.1660	↓0.34%	Gold	\$1815.80	↑0.35%
NIKKEI 225	28003.08	↑0.22%	Germany	-0.35	↓20.21%	€/£	1.1800	↓0.59%			
DAX 30	15540.31	↓0.94%	Japan	0.01	↓66.67%	£/¥	151.5100	↓1.06%			
CAC 40	6460.08	↓1.06%									

Figures quoted are in local currency.

Source: FE Analytics & Financial Times

Week Ahead

Monday – China: PBoC Loan Prime Rate

Tuesday – US: Building Permits (Jun)

Wednesday – US: Crude Oil Inventories

Thursday – Euro Area: ECB Interest Rate Decision (Jul)

Friday – UK: Services PMI

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